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Department of the Treasury  
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Refer Reply To:  
CC:PSI:B04 – PLR-136774-05

Date:  
March 19, 2007

In Re:

**Legend:**

Husband =

Wife =

Nominee Trust =

Schedule of Beneficiaries =

Property =

Individual 1 =

Individual 2 =

State =

Year 1 =

a =

b =

c =

d =

e =

f =

Trust =

Year =

Dear \_\_\_\_\_ :

This is in response to a letter dated July 5, 2005 and other correspondence, requesting rulings under §§ 2501, and 2702 regarding the proposed transfer of Parcel to Trust.

### Facts

The facts submitted and representations made are as follows. Husband and Wife are the beneficiaries of Nominee Trust under the Schedule of Beneficiaries of Nominee Trust. Individual 1 and Individual 2, individuals unrelated to Husband and Wife, are the trustees. Nominee Trust was formed for the purpose of acquiring fee simple title to Property for the benefit of Husband and Wife and becoming the recorded owner of Property.

Property has been held in Nominee Trust since Year 1, and has been used exclusively as the second residence of Husband and Wife since Year 1. Neither Property nor any structure on Property is rented out for commercial purposes.

Under the terms of Nominee Trust, either or both of the Husband and Wife may direct the trustees to terminate the trust. The termination becomes effective when the trustees file a certificate of termination with the registry of deeds. Upon termination of Nominee Trust, the trustees must convey Property to Husband and Wife as they direct.

Husband and Wife will direct the trustees of Nominee Trust to terminate the trust and convey to Husband and Wife fee simple title to Property as tenants by the entireties. Following this conveyance, Husband and Wife will subdivide Property into two parcels. Parcel, one of the two parcels resulting from the subdivision, will consist of approximately a acres of land on which the main living quarters and appurtenant structures are located. In addition to the main living quarters, the following structures are located on Parcel: (1) pool house of b square feet; (2) guest cottage of c square feet with no bedrooms or kitchen; (3) garage of d square feet; and (4) a barn of e square feet with two attached guest rooms which total f square feet and which are used by guests in the summer and by the Property's caretaker in the winter.

After the subdivision, Husband and Wife will execute Trust, which is intended to meet the requirements of a "personal residence trust" as described in §§ 25.2702-5(b)(1)-(3) of the Gift Tax Regulations. Under the terms of Trust, the trustees will hold Parcel (or any property acquired as a replacement personal residence) as the sole asset of Trust for the exclusive, rent-free use of Husband and Wife as their personal residence during their joint lives and until the death of the survivor of Husband and Wife. No additional contributions of assets may be made to Trust; however, if proceeds are payable to the trustees due to damage to, destruction of, or involuntary conversion of Parcel, the trustees may hold and invest those proceeds in one replacement personal residence within two years from the date of receiving the proceeds.

During the joint lives of Husband and Wife and the life of the survivor, all expenses of Parcel will be paid by Husband and Wife and the Purchasing Trust in the same manner in which expenses are borne by the holders of legal life estates and remainder interests under the law of State where Parcel is located. No person other than Husband and Wife will hold any term interest in Trust concurrently with either Husband or Wife. Upon the death of the survivor of Husband and Wife, the trustees of Trust will distribute Parcel to the trustees of Purchasing Trust to be added to the principal of Purchasing Trust. The initial trustees of Trust will be Individuals 1 and 2 and will be authorized to appoint additional or successor trustees and to remove trustees. Neither Husband nor Wife may serve as trustees, and only trustees who are not related or subordinate to either Husband or Wife within the meaning of § 672(c) of the Internal Revenue Code may be appointed as trustees.

After executing Trust, Husband and Wife will transfer Parcel to Trust in exchange for the transfer by Purchasing Trust to Husband and Wife of cash and marketable securities that have an aggregate fair market value on the date of transfer equal to the value of the remainder interest in Trust based on the fair market value of Parcel on the date of transfer (as determined by an expert appraiser) and the general actuarial principles of § 7520. The sale will be made pursuant to a written agreement executed by Husband and Wife and the trustees of Purchasing Trust.

Purchasing Trust was established by Husband in Year. The current and remainder beneficiaries of Purchasing Trust are Husband and Wife's issue, except that the trustee has the power, until the death of the survivor of Husband and Wife to distribute trust corpus to one or more charities as the trustee determines.

It is represented that neither Husband nor Wife is suffering from any condition or illness such that there is at least a 50 percent probability that either Husband or Wife will die within one year. Neither Husband nor Wife has ever transferred an interest in a residence in a transaction described in § 2702(a)(3)(A)(ii).

Taxpayers have requested the following rulings:

1. Parcel constitutes a "personal residence" for purposes of § 2702(a)(3)(A)(ii) and § 25.2702-5(b)(2).
2. The Taxpayers' sale of a remainder interest in Trust to the Purchasing Trust qualifies for the "personal residence trust" exception to the special valuation rule of § 2702(a)(2), and therefore the remainder interest should be valued for federal transfer tax purposes in accordance with the general actuarial valuation rules under § 7520.
3. Provided the Purchasing Trust pays for the remainder interest in Trust with cash or marketable securities having an aggregate fair market value equal to the value of the remainder interest determined in accordance with the general actuarial valuation rules under § 7520, the Taxpayers' sale of the remainder interest will constitute a sale for adequate and full consideration in money or money's worth and will not in any part constitute a gift for federal gift tax purposes.

Section 2501 imposes a tax on the transfer of property by gift by an individual. Section 2511 provides that the tax imposed by § 2501 applies whether the transfer is in trust or otherwise, whether the gift is direct or indirect and whether the property is real or personal, tangible or intangible.

Section 2512(a) provides that, if a gift is made in property, the value thereof at the date of the gift shall be considered the amount of the gift. Section 2512(b) provides that where property is transferred for less than an adequate consideration in money or money's worth, then the amount by which the value of the property exceeded the value of the consideration is deemed a gift.

Section 2702(a)(1) provides that solely for purposes of determining whether a transfer of an interest in trust to (or for the benefit of) a member of the transferor's family is a gift (and the value of such transfer), the value of any interest in such trust retained by the transferor or any applicable family member (as defined in § 2701(e)(2)) shall be determined as provided in § 2702(a)(2).

Section 2702(a)(2) provides that the value of any retained interest that is not a qualified interest is treated as being zero. The value of any retained interest that is a qualified interest is determined under § 7520.

Section 2702(a)(3)(A)(ii) provides that section § 2702(a)(2) shall not apply to any transfer of an interest in trust all the property in which consists of a residence to be used as a personal residence by persons holding term interests in such trust.

Section 25.2702-5(a)(1) of the Gift Tax Regulations provides, in part, that § 2702 does not apply to a transfer in trust meeting the requirements of that section. A transfer in trust meets the requirements of the section only if the trust is a personal residence trust as defined in section § 25.2702-5(b).

Section 25.2702-5(b)(1) provides that a personal residence trust is a trust the governing instrument of which prohibits the trust from holding, for the original duration of the term interest, any asset other than one residence to be used or held for use as a personal residence of the term holder and qualified proceeds (as defined in § 25.2702-5(b)(3)). Expenses of the trust whether or not attributable to trust principal may be paid directly by the term holder of the trust.

Section 25.2702-5(b)(2)(i) provides that a personal residence of a term holder is either the principal residence of the term holder (within the meaning of § 1034); one other residence of the term holder (within the meaning of § 280A(d)(1) but without regard to § 280A(d)(2)); or an undivided fractional interest in either.

Section 25.2702-5(b)(2)(ii) provides that a personal residence may include appurtenant structures used by the term holder for residential purposes and adjacent land not in excess of that which is reasonably appropriate for residential purposes (taking into account the residence's size and location).

Under § 25.2702-5(b)(2)(iii), a residence is a personal residence only if its primary use is as a residence of the term holder when occupied by the term holder. The principal residence of the term holder will not fail to meet these requirements merely because a portion of the residence is used in an activity meeting the requirements of § 280A(c)(1) or (4) (relating to deductibility of expenses related to certain uses), provided that such use is secondary to use of the residence as a residence. A residence is not used primarily as a residence if it is used to provide transient lodging and substantial services are provided in connection with the provision of lodging (e.g. a hotel or a bed and breakfast). A residence is not a personal residence if, during any period not occupied by the term holder, its primary use is other than as a residence.

Under § 25.2702-5(b)(2)(iv), if spouses hold interests in the same residence (including community property interests), the spouses may transfer their interests in the residence (or a fractional portion of their interests in the residence) to the same personal residence trust, provided that the governing instrument prohibits any person other than one of the spouses from holding a term interest in the trust concurrently with the other spouse.

Section 2702(c)(1) provides that for purposes of this section, the transfer of an interest in property with respect to which there is one or more term interests shall be treated as a transfer of an interest in trust.

Under §2702(c)(2) and §25.2702-4(c), for purposes of § 2702, if an individual acquires a term interest in property in the same transaction (or a series of related transactions) one or more members of the individual's family acquire an interest in the same property, the individual acquiring the term interests in the property is treated as having acquired the entire property and then transferring to the family members the interests acquired by such persons in the transaction (or series of transactions). The transfer is treated as made in exchange for the consideration (if any) provided by the family members for the acquisition of their interests in the property.

Section 2702(c)(3)(B) provides that the term "term interest" means either a life interest in property, or an interest in property for a term of years.

Section 25.2702-4(d), Example 2, considers a situation where K owns rental real estate valued at \$100,000. K sells a remainder interest in the property to K's child, retaining the right to receive the income from the property for 20 years. The purchase price paid by K's child for the remainder interest is equal to the value of the interest determined under § 7520. K's retained interest is not a qualified interest and is therefore valued at zero. Therefore, K has made a gift in the amount of \$100,000 less the consideration received from K's child.

Section 2702(e) provides that the term "member of the family" has the meaning given such term by § 2704(c)(2). Section 2704(c)(2) defines "member of the family" to mean, with respect to an individual, (A) such individual's spouse, (B) any ancestor or lineal descendant of such individual or such individual's spouse, (C) any brother or sister of the individual, and (D) any spouse of any individual described in clauses (B) or (C).

Section 7520(a) provides that the value of an annuity, an interest for life or a term of years, and a remainder or reversionary interest is to be determined under tables prescribed by the Secretary of the Treasury using the interest rate as prescribed under §7520(a)(2).

Ruling 1.

Based on the facts submitted and the representations made, the size of Parcel is comparable to that of properties in proximity to Parcel used for residential purposes. Accordingly, for purposes of § 25.2702-5(b)(2)(ii), Parcel includes adjacent land not in excess of that which is reasonably appropriate for residential purposes (taking into account the residence's size and location). In addition, the residence and appurtenant structures located on Parcel satisfy the primary use requirements of § 25.2702-5(b)(2)(iii). Accordingly, we conclude that Parcel constitutes a "personal residence" within the meaning of § 2702(a)(3)(A)(ii) and § 25.2702-5(b)(2).

Rulings 2 and 3.

In the instant case, Husband and Wife will transfer their respective interests in Parcel to Trust, and in a related transaction Husband and Wife will transfer a remainder interest in Parcel, under the terms of Trust, to Purchasing Trust in exchange for Purchasing Trust's payment to Husband and Wife of cash and securities equal in value to the actuarial value of the remainder interest as determined under § 7520. The transaction comes within the purview of § 2702(c)(2) and § 25.2702-4(c) and is similar to the transaction described in § 25.2702-4(d), Example 2, except that Example 2 does not involve a transfer to a personal residence trust. Therefore, the transaction is treated as a transfer by Husband and Wife of their respective remainder interests in Parcel coupled with the retention by each, under the terms of Trust, of a life interest in Parcel.

Assuming neither Husband nor Wife is terminally ill as that term is defined in § 25.7520-3(b)(3), Husband and Wife will each receive adequate consideration for the transfer of their respective remainder interest to Purchasing Trust. Further, assuming that Trust constitutes a "personal residence trust" that meets the requirements of § 25.2702-5(b)(1)-(3), Husband's retained interest and Wife's retained interest will be valued under the actuarial tables prescribed under § 7520. Accordingly, we conclude that, the transfer of Parcel to Trust followed by the sale of the remainder interest to Purchasing Trust in exchange for cash or marketable securities having an aggregate fair market value equal to the value of the remainder interest as of the date of transfer determined under the actuarial tables prescribed under § 7520, will not constitute a taxable gift by either Husband or Wife for federal gift tax purposes under § 2501.

Except as specifically ruled herein, we express no opinion on the federal tax consequences of the proposed transaction under the cited provisions or under any other provisions of the Code. Specifically, we express no opinion regarding whether the corpus of Trust will be includible in the gross estate of either Husband or Wife under § 2036. Further, we are expressing no opinion regarding the fair market value of Parcel on the date Parcel is contributed to Trust.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Sincerely yours,

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George Masnik, Chief  
Branch 4  
Office of Associate Chief Counsel  
(Passthroughs and Special  
Industries)

Enclosure

Copy for section 6110 purposes

cc: